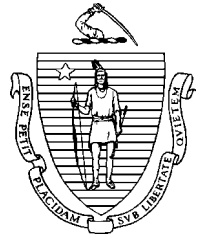




Commonwealth of Massachusetts State Ethics Commission

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CONFLICT OF INTEREST OPINION EC-COI-93-2

FACTS:

The ABC Hospital is a chronic disease hospital owned and operated by a county. A state statute authorized and directed the County Commissioners to construct a hospital for “the treatment of persons ill with tuberculous and other contagious diseases.” Subsequent Acts provided that the hospital could treat patients who were able to pay the County and patients from outside of the County, provided that priority be given to “poor patients who are under the care of public health departments within the County,” and permitted the hospital to also care for individuals with cancer and chronic diseases, including mental disorders. By statute, the hospital has a Board of Directors composed of the three County Commissioners, the County Treasurer, the County public health officer and six residents of the County appointed by the Commissioners.

In the late 1980’s, the County Commissioners decided to explore the possibility of terminating county management of the Hospital because of significant financial losses which the Hospital had sustained, as well as the difficulty in keeping abreast of the complex health care issues and health financing issues today. However, the County wanted to assure that rehabilitation care would continue to be available to the residents of the County.

The County hired a consultant to determine the feasibility of developing a private rehabilitation hospital. When the consultant determined that such a hospital was feasible, it prepared a determination of need application, financed by the County, to submit to the Department of Public Health. (The County hopes to be reimbursed the expense of the application at some time by the non-profit organization). A determination of need was granted for construction of a 60-bed comprehensive inpatient and outpatient rehabilitation facility on the existing Hospital site.

The County Commissioners were authorized to negotiate with a non-profit organization which was organized to establish a private, non-profit rehabilitation hospital. The County Commissioners were authorized to enter a Ground Lease, as well as other instruments to lease or sell the County buildings. The lease is “for the purpose of establishing on the ground-leased parcel a new hospital ... to provide special care, rehabilitation and other medical services.” The lease is required to contain provisions giving priority in admitting patients to residents of the County and its neighboring counties, permitting members of the County Commissioners to participate in meetings of the non-profit Board as non-voting attendees, and providing that space in the new facility be made available to state, county, municipal, and other government entities to provide medical and social services to the population, if necessary. The County may subordinate its interest in the Ground Lease to the financing institution to facilitate the ability of the non-profit organization to obtain financing.

With the impetus of the consultant, a non-profit organization was created. The purpose of the non-profit is “to establish and maintain a special care and rehabilitation hospital on a tract of land owned by the County and to provide such other medical services and activities as are related to the needs and purposes of the hospital.”

According to the non-profit organization’s bylaws, the Board of Directors will include two residents of the County, one resident or employee of three neighboring counties, three designees of area hospitals, and seven designees of the consultant. The trustees may, by majority vote, elect other trustees or fill vacancies. The President, Treasurer and Clerk of the organization are elected annually by and from the trustees. The County Commissioners made recommendations concerning probable candidates to serve on the initial Board, but the County did not appoint any members of the first board.

The County Commissioners and the non-profit organization have entered an Agreement to Ground Lease which memorializes the relationship of the parties. The non-profit organization will develop, construct and operate a new rehabilitation hospital and in the process may demolish, or renovate existing buildings or construct a new physical facility pursuant to the terms of the ground lease. If existing buildings are required to be renovated or demolished the County may either execute a quitclaim deed or lease the buildings on mutually acceptable terms. It is anticipated that the buildings will be conveyed or leased for nominal consideration.

The County has the right to review and approve the final design plans, including exterior design, placement of parking areas, utilities, height design and siting of every element of the hospital and landscaping. The County has approval rights of all architects, engineers and general contractors on the site. The County has the right to be notified before the non-profit applies for licenses, permits and approvals and the County will assist in obtaining such licenses and permits, if the non-profit agrees to pay the County's out of pocket costs. The County has the right to approve the terms of the mortgage obtained for the project financing. The County will not guarantee or underwrite any obligation of the non-profit corporation.

Members of the Board of County Commissioners will sit as non-voting attendees at Board meetings in order to monitor progress on construction and the transfer of patients to the new non-profit hospital as a result of the County's decision to close the current Hospital. The non-profit corporation will also use its best efforts to lease space to the County for the County's provision of medical services.

Under the lease, the consent of the County Commissioners must be obtained to any sub-lease, assignment, or transfer but consent will not be withheld if the transfer is to another non-profit. The County has right of first refusal if the hospital is sold. The County Commissioners have the right to approve any sale. At the termination of the lease, title to all physical structures, other improvements and all appurtenances will revert (with or without cost) to the County. The initial ground rent will be based upon the fair market value of the premises as determined by a disinterested professional appraiser or such lesser rent as the County may agree to.

The non-profit Board must receive the consent of the County Commissioners (which consent will not be withheld if another non-profit is involved) prior to merging, combining or affiliating with a person or organization; entering into a partnership or joint venture with a person or organization; transferring all or substantially all of the assets of the non-profit to a person or organization; altering or amending the non-profit's organizational documents so that voting control is modified; changing its corporate membership or trustees so that voting control is altered. The County Commissioners have the right to consent to any transfer of the non-profit's rights under the lease. The non-profit may not amend the determination of need without the consent of the County Commissioners.

QUESTION:

Under G.L. c. 268A will the non-profit corporation be considered to be a "county agency"?

ANSWER:

No.

DISCUSSION:

The issue before the Commission is whether the new non-profit corporation, which will be the lessee under the Ground Lease with the County, is a "county agency" for purposes of G.L. c. 268A. G.L. c. 268A, §1(c) defines "county agency" as "any department or office of county government or any division, board, bureau, commission, institution, tribunal or other instrumentality thereof or thereunder." G.L. c.268A, §1(c).

Thus, we are required to consider whether the non-profit organization is an "instrumentality" of the County. The Commission does not consider the corporate structure of an entity to be dispositive of the issue. Rather, we weigh such factors as: whether an entity is created by governmental means; whether the entity serves an inherently governmental purpose; whether the entity is controlled or supervised by government employees; and whether the entity is funded by the government or expends government funds. *See EC-COI-91-12; 89-1; 88-24; 88-19.*

Recently, the Massachusetts Appeals Court has had the opportunity to interpret the term “instrumentality” in conjunction with analogous language within the definition of “municipal agency” and employed an analysis similar to that of the Ethics Commission. *McMann v. State Ethics Commission*, 32 Mass. App. Ct. 421 (1992). In reaching the conclusion that a regional school district is an instrumentality of each municipal member under G.L. c. 268A, §1(f), the Court considered the ordinary and approved use of the word “instrumentality” in the statute; the formation, operation and purpose of a regional school district; and the purpose of G.L. c. 268A. *Id.* at 425-428. The Court found that the municipalities use the school district as a means to fulfill their statutory obligation to provide education, that the municipalities delegate their statutory educational duties to the school district, that the municipalities played a substantial role in the creation of the district and in the district’s financial matters, and that the municipalities fund the district. *Id.* at 427. The Commission’s recent jurisdiction opinions have expressly followed the Appeals Court’s analysis in the *McMann* case. *EC-COI-92-40*; *92-27*; *92-26*.

Applying this precedent to the non-profit corporation, we conclude that the corporation lacks sufficient indicia of a government entity to be considered a “county agency.” Initially, in order to determine jurisdiction, we have examined the presence or lack of a statute, rule, regulation, or other direct agency action in furtherance of its statutory mandate in the creation of a non-profit organization. *See EC-COI-91-12* (agency passed resolution to assist in creating non-profit organization); *90-3* (primary purpose on non-profit to provide fundraising support to University furthering legislatively mandated purpose); *88-24* (non-profit created by the agency to administer its statutory mandate). The non-profit hospital corporation was not established by statute, rule or regulation but rather by private parties. The County Commissioners were authorized to enter a lease with a non-profit corporation, not specifically to create the corporation. In the past, we have been reluctant to find jurisdiction where a non-profit corporation is created in response to a private contract or other private action. *See EC-COI-88-19* (no jurisdiction where stems from a private contract, notwithstanding the participation of governmental officials in organizational efforts); *84-65* (no jurisdiction where entity created pursuant to terms of a private will); *compare EC-COI-90-7* (government creation found where there was indirect legislative authorization to formulate a trust agreement).

However, we note that the County created the need for the non-profit corporation, in a preliminary management agreement with the consultant, had substantial input into the initial determination to create the non-profit corporation and had obtained the determination of need so that the project would be viable. We also note that the non-profit corporation is assisting the County in fulfilling its statutory mandate to provide medical care to County residents, although the scope of the new hospital’s services is significantly greater than the County’s mandate, which is to provide chronic care. *See EC-COI-84-76*, n.7 (although a non-profit corporation was chartered by act of General Court, its purpose is not an essentially governmental function). Thus, the factors relating to governmental creation and purpose are not clear in these circumstances; however, we do not find it necessary to resolve these issues in light of the conclusions we reach under the remaining factors.

We do not find that the corporation will expend or receive county funding. The corporation is required to seek private financing to build the new hospital and will pay a fair market rental under the lease. Although the County may subordinate its interest in the ground lease to the private financing institution, it will not guarantee or underwrite any of the new hospital’s obligations. *See EC-COI-84-76*, n.7 (factor in not finding jurisdiction was that non-profit required to raise own revenues and may not pledge Commonwealth’s credit). The County also expects to be reimbursed for expenses it has accrued to date in obtaining the determination of need.

Finally, the factor which we consider to be the most significant basis of our conclusion in this case is the lack of county governmental control over the new hospital. *See EC-COI-92-1*; *91-12*. The Commission has traditionally examined the nature of governmental control exercisable over an entity’s internal operations through government participation in the selection of the non-profit’s Board of Directors or the presence of a bloc of government employees on the Board who are capable of controlling Board actions. *See e.g., EC-COI-91-12* (government presence on Board not sufficient to control Board decisions and no jurisdiction found); *90-3* (potential for government control of Board decisions); *89-1* (same); *89-24*. While there is governmental regulation by the County over the non-profit corporation by virtue of the lease arrangement, the purpose of this oversight is to protect the County’s investment and rights under the contract and is not control over Board decisions or supervision over the administration and operation of the hospital. Under the hospital corporation bylaws, the County Commissioners may participate at Board meetings only as non-voting attendees and no county employee may serve as a Board member during county employment. Unlike the current County Hospital Board, the County Commissioners did not select the initial new hospital Board and do not have the authority to select future

members. *See EC-COI-88-19; 84-76, n.7.*

In conclusion, the scope and nature of control exercisable by the County, and the lack of public funding, are sufficient to find that the non-profit corporation is not an instrumentality of the County and, thus not a “county agency” for purposes of G.L. c. 268A, §1(c).

DATE AUTHORIZED: January 26, 1993